

आयकर अपीलिय अधिकरण, 'डी' न्यायपीठ, चेन्नई
IN THE INCOME-TAX APPELLATE TRIBUNAL 'D' BENCH, CHENNAI
श्री वी दुर्गा राव न्यायिक सदस्य एवं श्री जी. मंजुनाथा, लेखा सदस्य के समक्ष
Before Shri V. Durga Rao, Judicial Member &
Shri G. Manjunatha, Accountant Member

आयकर अपील सं./I.T.A. No. 944/Chny/2015
निर्धारण वर्ष/**Assessment Year:2010-11**

M/s. YCH Logistics (India) Private Limited, Plot No. DV1, SIPCOT Hi-Tech SEZ, Phase II, Sirumangadu Village, Sriperumbudur Taluk, Kancheepuram District, Tamil Nadu 602 105. [PAN:AAACY2873L] Vs. The Deputy Commissioner of Income Tax, Corporate Circle 3(2), Chennai.

(अपीलार्थी/Appellant)

(प्रत्यर्थी/Respondent)

अपीलार्थी की ओर से / Appellant by : Shri Ajit Kumar Jain, CA
प्रत्यर्थी की ओर से/Respondent by : Shri S. Palanikumar, CIT
सुनवाई की तारीख/ Date of hearing : 07.07.2022
घोषणा की तारीख /Date of Pronouncement : 30.08.2022

आदेश /O R D E R

PER V. DURGA RAO, JUDICIAL MEMBER:

This appeal filed by the assessee is directed against the assessment order passed under section 143(3) r.w.s. 144C(5) of the Income Tax Act, 1961 ["Act" in short] dated 14.01.2015 relevant to the assessment year 2010-11.

2. Brief facts of the case are that the assessee is engaged in the business of providing logistics services and filed its return of income on 20.07.2011 for the assessment year 2010-11 admitting loss of

₹.3,76,22,427/-. The return of income filed by the assessee was processed under section 143(1) of the Act. Subsequently, the case was selected for scrutiny under CASS and notice under section 143(2) of the Act was issued on 25.08.2011. Later, a notice under section 142(1) along with questionnaire was issued. In response, the assessee filed various details as called for. During the course of assessment proceedings, on perusal of the details furnished by the assessee, the Assessing Officer has noted that the value of international transactions of the assessee has exceeded the prescribed limit, the reference was made to Id. TPO for proper determination of arm's length price in relation to international transactions entered into during the financial year 2009-10 with its associated enterprises. After considering the details of documents and information furnished by the against notice issued by the Id. TPO-VI under section 92CA(2) of the Act, the Id. TPO-VI considered that the ALP for the management services or admin services said to be rendered by the AE is NIL and consequently vide order dated 20.01.2014, the Id. TPO has recommended for a downward adjustment of ₹.5,85,78,200/- to the AE cost.

3. The assessee filed its objection before the Id. DRP. After considering the detailed submissions of the assessee, the Id. DRP has

observed that the assessee has not substantiated the nature of expenditure with reference to need-evidence-benefit with documentary proof and therefore, confirmed the action of the TPO in making the downward adjustment.

4. On being aggrieved, the assessee is in appeal before the Tribunal. The Id. TPO/Id. DRP has merely held that the ALP of the transaction is Nil without even identifying comparables which is not in accordance with the methodologies provided in the Rules. The Id. Counsel has further submitted the Id. TPO/Id. DRP have erroneously considered the management support services received by the assessee as in the nature of 'shareholding activity' and concluded that the management support services received did not confer any benefit to the assessee. It was further submission that no such adjustment was made in the TPO's order for the earlier assessment years 2008-09 and 2009-10. The Id. AR, also relied on the following judgments, wherein it has been held that no transfer pricing adjustment is warranted in a scenario where the TPO has not taken any step to identify a comparable to determine the ALP :

- a. *Merck Ltd. vs. DCIT (148 ITD 513 - Mumbai, ITAT) – upheld by Bombay High Court [ITA 272 of 2014]*
- b. *DCIT vs. Flakt India Ltd. in ITA No.1032/Mds/2014 dated 09.06.2016 – Chennai ITAT*

- c. *Siemens Gamesa Renewable Power Pvt. Ltd. v. DCIT in ITA Nos. 1420 & 376/Mds/2017 dated 13.11.2017 – Chennai ITAT*

Applying the above principles to the current fact pattern, the Id. Counsel for the assessee has submitted that the action of the TPO in determining the ALP to be NIL without even identifying a comparable transaction is inappropriate and therefore, the transfer pricing adjustment in this regard needs to be set aside.

5. On the other hand, the Id. DR has submitted detailed written submissions and the same are reproduced as under:

YCH Logistics India Private Limited (YCHIPL) was incorporated in September, 2002. The company was promoted as a wholly owned subsidiary by YCH Group Pte Limited, Singapore.

YCHIPL is primarily engaged in providing services like Supply Chain Management (SCM), Vendor Managed Inventory (VMI) etc. The company is the sole SCM company for both raw materials and finished goods for Dell India and its operational activities as VMI is for the Vendors of Dell India.

During the year the assessee company had paid Rs.5,85,78,200/- as IT Support / management fees to its AE, M/s. YCH Group Pte Ltd, Singapore. The total turnover of the company is Rs. 65.07crore and hence the management fees payment turns to be 9% to sales turnover.

In transfer pricing wherever it is possible it is important to benchmark the AE transactions separately for a better comparability. The assessee may have many transactions viz., Sales, purchases loan, guarantee, etc., but combining them and studying under a single method would not be fit to call as "Most Appropriate Method". The term 'Most Appropriate method' is of high superlative language i.e., given the choice between various methods, the assessee has to select a method which would give a closest proximity to the ALP value. In such a scenario, combining all the AE transactions and studying under TNMM is not a Most Appropriate Method. The project management cost has to be benchmarked separately by analyzing the each actual services received by the assessee company. Hence TNMM selected by the assessee to benchmark project management cost is hereby rejected and CUP is adopted as Most Appropriate Method by the TPO.

Most of the email correspondences are routine in nature and reflecting day to day communication between the assessee and the parent company. These are in

the nature of raising doubts, seeking guidance, review, updating the sales, enquiry about the general functions of the company. In any case, a shareholder has to perform these functions since it had investment stake in the company. These shareholder's services categorized as 'Stewardship Services' do not require separate payment as per the OECD guidelines.

The AR in their TP documentation had categorically stated that the assessee company does the following key functions.

- 1. Determines the clearing and forwarding agents.*
- 2. Arranges for freight and insurance*
- 3. Providing inventory service*
- 4. Supervises the supply chain management*
- 5. Plans investment in warehouse and handling equipments*
- 6. Delivers the products to the customer*

The assessee company had also submitted that they have/own trained personnel to carry out the above key functions. If the assessee company has trained personnel and the assessee company performs all the key managerial functions, the necessity to avail such managerial services remains unexplained.

In this regard kindly note the following OECD guidelines (Para No.7.9; Page No:207) "In a narrow range of such case, an intra, group activity may be performed relating to group members even though those group members do not need the activity (and would not be willing to pay for it were they independent enterprises). Such an activity would be one that a group member, i.e. in its capacity as shareholder. This type of activity would not justify a charge to the recipient companies"

Further, the Hon'ble ITAT in the following cases had clearly had held that the ALP of management services fee paid as NIL on grounds that only incidental and passive association benefits are received by the Indian company from its AE and the volume of the benefits are not in commensurate with the payment made by the Indian Company.

1) ITA No.5097/Del/2011 AY - 2007-08 M/s. Knorr Bremse India Ltd. Vs. ACIT Faridabad (ITAT 'T Bench, New Delhi)

2) ITA No.352/Bang/ /2009 AY 2003-04 M/s. Gemplus India P Ltd Vs. ACIT, Circle II (4), Bangalore (ITAT "A:' Bench, Bangalore)

The AR had submitted that the provision of management fees is inextricably linked with the logistics business and hence TNMM is the Most Appropriate Method. Further it was submitted the TNMM is more tolerant to financial differences.

In this regard it has to be noted that in transfer pricing, wherever it is possible it is better to benchmark the "International Transactions" separately. The transaction to transaction approach is the most preferred. The assessee company transacts both with AEs and non AEs. It may not be possible to identify exactly whether the profit had arisen due to the transactions with AE (or) non AE. In this context, the I.T. Act prescribes 5 different methods without mentioning the priority of

the methods. Sometimes, the tested party may operate in a high end service segment and just comparing with low end business segments/companies is not enough. The Real profit might have been deflated in these cases. There are lots of possibilities that a company may shift the profits (or) siphon off the funds to their AE after reaching the margins similar to that of in the low end business/ services companies. Hence it is imperative that AE payments viz., Royalty, trademark fees, management fees, purchase/sale etc., has to be benchmarked separately.

In the case of Development Consultants Pvt. Ltd. Vs DCIT (115 TTJ 577 (2208) it was held that Arm's Length Price should be determined on a transaction by transaction basis. Only in cases when the separate transactions are so closely linked or continuous that they cannot be evaluated adequately on a separate basis, such transaction may be evaluated together.

In the case of Star India Pvt. Ltd. Vs ACIT Range XI(I), the Hon'ble Mumbai Tribunal ITA No. 3585/M/2006 (!TAT Mumbai), it was held that the ALP should be determined on a transaction by transaction basis with respect to the functions performed, assets employed and risk assumed by the assessee and ALP cannot be determined on a consolidated basis.

From the above, it is clear that instead of aggregating transactions and adopting TNMM, individually analyzing each transaction and adopting CUP method would be the most suited. As per OECD guidelines 1.42 "ideally, in order to arrive at the most precise approximation of fair market value, the Arm's Length principle should be applied on a transaction by transaction basis ', The Income Tax Act also prescribes 5 different methods precisely to address these issues. Based on the relevant transactions with the AE, the most appropriate method needs to be identified and benchmark the transactions accordingly.

In the above context, the assessee needs to submit the relevant documentary evidences and prove that such documentary evidences should indicate that some valuable services (involving cost element to the AE) was actually received by the assessee company. From documentary evidences submitted it was already noted that these communication had arisen only due to the passive association with AEs. The documentary evidences are in the nature of seeking guidance, enquiries, reviews, providing information, which had arisen only due to the passive association with the AEs. In any case a shareholder has to perform these routine activities to have a better control over his investment.

The assessee company's organization consists of:

- *Director -: Sales*
- *GM - Risk & Insurance*
- *Country Head*
- *Corporate Operations*
- *GM-SRM*
- *Finance Director*
- *Executive Director*

Kindly note that the above structure is definitely not a lower level employee structure.

The assessee had accepted that the operations are receiving, providing suggestions, monitoring etc. The AR had not filed any details regarding the cost incurred by the AE, cost contribution analysis for the group less the stewardship cost etc.

The European Union Joint Transfer Pricing Forum (JTPF), in their summit at Brussels on 04.02.2010 on the "Guidelines on low value adding Intra-Group Services" had given a non-exhaustive list that includes OECD elements and additional services that the JTPF reviewed and recognized as ones that are regularly classified as shareholder costs. The relevant para is extracted as below:

Description of costs to be considered as shareholder costs	Comments
12.d Costs of managerial and control (monitoring) activities related to the management and protection of the investments in participation unless an independent party would, have been willing to buy or to perform for itself?	Generally to be considered as Shareholder costs
6. b Costs relating to reporting requirements of the parent company including the consolidation of reports	Shareholders costs
14.2.2 Costs for drafting and auditing of the financial statements of the subsidiary in accordance with the accounting principles of the States of the parent (e.g. US GAAP)	Shareholder costs, unless such activity has a positive effect for the activity of the subsidiary on its own and simply because it is part of the group. This may be the case where the financial statement drafted by applying the accounting principles of the parent company is used by the parent company itself to render specific services to the subsidiary, as market analysis, budgeting, etc.
19.g Investor's relations' costs of the parent company: Costs for press Shareholders costs conferences and other communications with (i) shareholders of the parent company, (ii) financial analysis, (iii) funds and, (iv) other stakeholders of the parent company.	
22.j Other activity you identify as shareholder activity: Activities relating to the adoption and enforcement with statutory rules and rules of conduct with regard to "corporate governance" by the parent company itself or the group as a whole.	Shareholders costs

Here again, it was clearly stated that the reporting requirements and cost of control and monitoring are shareholder costs and cannot be shifted to the assessee. As seen from the above table, the OECD mandates that the above costs pertains to

shareholders only and cannot be reimbursed from the receiver of these services. Most of the services claimed by the assessee as management services and clearly falls under the provisions of the above table.

In the case of Gemplus India Pvt. Ltd. vs ACIT Circle 11(4), Bangalore. ITA No. 352/Bang/09, the Hon'ble ITAT had held that the payment on account of management services should commensurate with the volume and the quality of the services received. The term "quality" used by the Tribunal is very important and have a wider meaning. It is important to note here that the decision was rendered with the given fact that the Gemplus was only having a handful of employees with them. In the case of assessee company they have a structured hierarchy in place with various level of managerial persons with them. The facts submitted in the earlier paragraphs and the facts observed in the show cause notices is sufficient to prove that these services would not demand such huge payment and the ALP needs to be adjusted suitably. The ITAT had observed that "This is a vital observation made by the TPO which goes to the root of the issue. The function of the TPO is to compare the payments made by the assessee company for services received if any and to see whether those payments are comparable. In a given scenario, the TPO has to examine whether the payments were ALP conducive. Therefore it is very imperative on the part of the assessee to establish before the TPO that the payments were made commensurate to the volume and quality of services and such costs are comparable". The need- evidence- benefit test was not substantiated in the present case by the AR.

In the case of M/s. Knorr Bremse India Ltd. Vs. ACIT Faridabad (ITAT "I" Bench, New Delhi ITA No.5097/Del/2011) - it was held that only passive and incidental benefits were received by the assessee and ALP was determined as nil. In this case the Hon'ble ITAT had also emphasized the necessity on the part of the assessee to maintain the relevant records required under Rule 10D(l) in order to determine the ALP.

It was clearly observed that the payment of Rs.5,85,78,200/- (9% on sales) is not commensurate with the volume of the services rendered and the said communication had arisen only due to the passive association with the AEs and benefits said to be received are incidental in nature only.

Rule of consistency:

For the assessee's stand that the TPO has erred in disregarding the principle of consistency, it is stated that the ALP would vary based on the facts and circumstances of the case, uncontrolled transaction taken for the study, + / - 5 computations in each year. When such diverse factors play a role in determination of the ALP, the AR's submission regarding Rule of consistency is not applicable here.

6. We have heard both the sides, perused the materials available on record and gone through the orders of authorities below including paper

book and case law relied upon. It was case of assessee that, centralization of costs leads to significant group cost savings. It would be difficult for the assessee to procure the services from third party service providers which are specific to the group and products. Given that the services are peculiar and can be rendered only by the AEs by way of pooling the resources at group level, the contention of the learned TPO that it is merely in the nature of shareholder activity is baseless. Further, due to confidentiality issues, it is the general practice to undertake such services through group entities. The assessee has further contended that it has substantiated that the services have actually been rendered by its AE and established the underlying benefit derived out of such services. The Need Benefit Analysis on account of management service has been tabulated in page 36 to 42 evidencing each service provided by YCH Singapore to the assessee has resulted in significant benefit to the assessee. Therefore, the contention of the learned TPO and DRP that there is no requirement to avail management service from its AE is inappropriate. Further, the assessee has submitted the copy of various mail correspondences which evidences rendition of management services by its AE. Sample mail correspondences and reports shared by the AE evidencing the actual rendition of management service are furnished and the TPO also reproduced in his order. In this regard, the Id. Counsel

relied upon the decision of the Delhi Benches Tribunal in the case of Showa India (P) Ltd. v. DCIT in ITA No.166 of 2013 dt. 30.06.2016.

7. For the purposes of benchmarking the profits, the assessee has considered TNMM as the most appropriate method and the PLI of the assessee is higher than that of the comparable companies. In the case of Durr India (P) Ltd in ITA. No. 754/Mds/2014 dated 21.12.2016, the co-ordinate Bench of Tribunal has held that allocation of cost partly on the basis of turnover and net profit cannot be considered as a factor to propose transfer pricing adjustment. Further, it was held that where the PLI of the assessee under TNMM is at arm's length and it is not possible on the part of the department to identify a comparable, which is rendering similar services, the question of considering CUP method would not arise at all. Since the assessee has stated that all the relevant evidences were already available with the Assessing Officer/TPO and on that basis; it is required to be verified with regard to availing actual services and its allocation of cost to the assessee. Accordingly, this ground relating to Management fees is remitted to the file of the Assessing Officer for fresh consideration and the Assessing Officer after going through the evidences filed by the assessee decide the issue fresh as indicated

above. This ground of appeal of the assessee is allowed for statistical purposes.

8. So far as corporate tax issue raised in the appeal of the assessee relates to exclusion of freight charges incurred in foreign currency from export turnover. On perusal of the details submitted by the assessee, the Assessing Officer has observed that there is a payment of ₹.33,73,216/- in profit & loss account towards communication expenses (telephone & mobile charges) under the head 'Administrative expenses'. Further, para 19 of 'notes on accounts' it was noted that the assessee has incurred an expenditure of ₹.16,09,01,489/- in foreign currency towards management fees, travelling expenses, freight charges, internet & intranet charges and other expenses. Since the assessee was rendering services outside India, the Assessing Officer excluded the expenditure incurred in foreign currency from export turnover for the purpose of deduction under section 10AA of the Act. As the communication expenses as well as expenditure incurred in foreign currency are common expenditure for both SEZ and non-SEZ unit, the Assessing Officer has apportioned the expenditure totalling to ₹.16,42,74,705/- between SEZ unit and non SEZ units in the proportion of the respective total turnovers. The Apportionment of expenditure is as under:

Unit	Turnover	Percentage	Apportionment (in Rs.)
SEZ	20,21,70,117	31%	5,09,25,159/-
Non SEZ	44,88,65,807	69%	11,33,49,546/-
Total	65,10,35,923	100%	16,42,74,705/-

Accordingly, the Assessing Officer excluded the expenditure of SEZ unit of ₹.3,53,45,175/- from export turnover for deduction under section 10AA of the Act after obtaining recomputation of export turnover from the assessee.

9. However, vide order dated 16.12.2014, the Id. DRP has directed the Assessing Officer to exclude the expenditure in telecommunication charges & expenditure in foreign currency from the total turnover as well as export turnover. Accordingly, the Assessing Officer determined the deduction under section 10AA of the Act at ₹.4,72,45,473/- and brought to tax.

11. On being aggrieved, the assessee is in appeal before the Tribunal. The Id. Counsel for the assessee has submitted that the freight charges incurred in foreign currency in relation to its non SEZ unit from export turnover by treating the said expenses as incurred in connection with rendering of services outside India by the SEZ unit is not correct and prayed for deleting the addition.

12. On the other hand, the Id. DR supported the assessment order.

13. We have heard both the sides, perused the materials available on record and gone through the orders of authorities below. In the draft assessment order, the Assessing Officer has excluded the communication expenditure and expenditure incurred in foreign currency while working out deduction under section 10AA of the Act. The Assessing Officer has reduced the expenditure of ₹.3,03,33,568/- incurred in foreign currency from the export turnover. Before the Id. DRP, the assessee has contended that the expenditure in foreign currency and communication expenses are not included in export revenue and hence no exclusion is called for while arriving at the export turnover for deduction under section 10AA of the Act. After considering the submissions of the assessee and by following the Special Bench decision of the Tribunal in the case of ITO v. Sak Soft Ltd. 121 TTJ 865, the Id. DRP has directed the Assessing Officer to exclude the expenditure incurred in foreign currency and communication expenses from the numerator and the denominator for the purpose of computation of deduction under section 10AA of the Act. Accordingly, in view of the directions of the Id. DRP, in the assessment order, the Assessing Officer has recomputed the deduction under section 10AA of the Act at ₹.4,72,45,473/-.

14. The case of the assessee is that the Assessing Officer has apportioned freight charges and other expenditure incurred in foreign currency in SEZ and non-SEZ units and recomputed 10AA deduction. It was the explanation of the assessee that freight charges and other expenditure incurred in foreign currency is for non-SEZ units only. It was further submission that the assessee has been maintained separate books of account. Thus, the facts are contradictory. Therefore, we remit the issue back to the Assessing Officer to examine the claim of the assessee and to compute the 10AA deduction in accordance with law after affording an opportunity of being heard to the assessee.

15. In the result, the appeal filed by the assessee is allowed for statistical purposes.

Order pronounced on the 30th August, 2022 in Chennai.

Sd/-
(G. MANJUNATHA)
ACCOUNTANT MEMBER

Sd/-
(V. DURGA RAO)
JUDICIAL MEMBER

Chennai, Dated, 30.08.2022

Vm/-

आदेश की प्रतिलिपि अग्रेषित/Copy to: 1. अपीलार्थी/Appellant, 2. प्रत्यर्थी/
Respondent, 3. आयकर आयुक्त (अपील)/CIT(A), 4. आयकर आयुक्त/CIT, 5.
विभागीय प्रतिनिधि/DR & 6. गार्ड फाईल/GF.